

Oil and gas taxation in India
Deloitte taxation and
investment guides



Contents

1.0	Summary	1	6.0	Transactions	6
2.0	Corporate income tax	1	6.1	Capital gains	6
	2.1 In general	1	6.2	Sharing arrangements and farm outs	6
	2.2 Rates	2	7.0	Withholding taxes	7
	2.3 Taxable income	2	7.1	Dividends	7
	2.4 Revenue	2	7.2	Interest	7
	2.5 Deductions and allowances	2	7.3	Royalties	7
	2.6 Losses	3	7.4	Foreign tax treaties	7
	2.7 Foreign entity taxation	3	8.0	Indirect taxes	7
3.0	Other corporate income tax	3	8.1	Services tax	7
	3.1 Minimum alternate tax	3	8.2	Import, export, and customs duties	8
	3.2 Dividend distribution tax	3	8.3	Excise tax	8
	3.3 Tax on distributed income of domestic company for buy-back of shares	4	8.4	VAT, GST and Sales & Use	9
	3.4 Wealth tax	4	9.0	Other	9
4.0	Tax incentives	4	9.1	General anti-avoidance rules	9
	4.1 Research and development	4	9.2	Controlled foreign corporations	10
	4.2 Profit linked incentives	4	9.3	Royalty/profit sharing	10
	4.3 Investment linked incentives	4	9.4	Choice of business entity	11
	4.4 Other incentives	5	9.5	Foreign currency	11
5.0	Payments to related parties	5	10.0	Oil and gas contact information	12
	5.1 Transfer pricing	5			
	5.2 Thin capitalization	6			
	5.3 Interest deductibility	6			

Deloitte taxation and investment guides
www.deloitte.com/taxguides
Oil and gas tax guide

Tax professionals of the member firms of Deloitte Touche Tohmatsu Limited have created the Deloitte International Oil and Gas Tax Guides, an online series that provides information on tax regimes specific to the oil and gas industry. The Guides are intended to be a supplement to the Deloitte Taxation and Investment Guides, which can be found at www.deloitte.com/taxguides. For additional information regarding global oil and gas resources, please visit our website: www.deloitte.com/oilandgas

1.0 Summary

The principal Indian tax rates applicable to companies in the oil and gas industry are summarized in the following table:

	Basic tax rate	Surcharge, applied on tax	Cess, applied on tax and surcharge	Effective tax rate
Domestic companies				
Income > INR 100 million	30%	10%	3%	33.99%
Income > INR 10 million but not exceeding INR 100 million	30%	5%	3%	32.445%
Income < INR 10 million	30%	--	3%	30.90%
Foreign companies*				
Income > INR 100 million	40%	5%	3%	43.26%
Income > INR 10 million but not exceeding INR 100 million	40%	2%	3%	42.024%
Income < INR 10 million	40%	-	3%	41.20%
Minimum Alternate Tax				
Income > INR 100 million	18.5%	10%**/5%***	3%	20.96%/20.01%
Income > INR 10 million but not exceeding INR 100 million	18.5%	5%**/2%***	3%	20.01%/19.44%
Income < INR 10 million	18.5%	-	3%	19.06%
Dividend Distribution tax****				
Dividend distributed	15%	10%	3%	16.995%

* Presumptive taxation applies to foreign companies engaged in the business of providing services or facilities, or supplying or hiring plant or machinery used in connection with the prospecting, extraction or production of petroleum and natural gas – 10% of the amounts received as consideration for the aforesaid services is taxable on a presumptive basis (i.e. the taxable income is computed as a percentage of gross income, without any regard to actual expenses incurred in earning the income).

** For domestic companies.

*** For foreign companies.

**** Dividends subject to Dividend Distribution Tax will be exempt in the hands of the shareholder, regardless of residential status of the shareholder.

2.0 Corporate income tax

2.1 In general

Domestic companies are taxed on their worldwide income. A foreign tax credit can be claimed to provide relief against double taxation if the income of the domestic company has suffered tax overseas.

If a Production Sharing Contract (“PSC”) with the Government of India is applicable, deduction for expenses can be claimed either in the year of commercial production, or can be amortised over ten years from the date of first commercial production by companies that are engaged in exploration, extraction and production activities of petroleum and natural gas. The deduction and allowances as applicable to the oil and gas industry are discussed in detail in Section 2.5 below.

There are no ring-fencing provisions under either the domestic tax laws or under the PSC. It is therefore possible to deduct expenses of a particular oil and gas block against the income of other oil and gas blocks.

As per the notification dated 8 March 1996 issued by the Central Board of Direct Taxes section 293A, persons who have entered into agreements with the Government for the extraction of mineral oils will not be assessed to tax as Association of Persons.

The current Indian tax legislation is proposed to be replaced by the Direct Taxes Code which is currently under discussion. The changes proposed by the Direct Taxes Code are provided in Section 9.2 below.

There are no ring-fencing provisions under either the domestic tax laws or under the PSC. It is therefore possible to deduct expenses of a particular oil and gas block against the income of other oil and gas blocks.

2.2 Rates

Please refer Section 1.0 – Summary for the Indian tax rates as applicable to domestic companies.

2.3 Taxable income

The taxable income of domestic companies is computed by making certain adjustments to the profits as per company accounts. The adjustments generally relate to depreciation, expenses on which applicable withholding tax has not been deducted and statutory dues paid after the prescribed due dates, etc.

2.4 Revenue

Income is a broad concept and has been defined in domestic tax law in an inclusive manner. Some of the common income items in the oil and gas industry include the sale of oil and the transfer of licenses, or participating interests in oil and gas assets.

There has been controversy on the taxability of mobilization/demobilization charges paid to a foreign company towards transportation of plant and machinery from outside of India to locations in India or its territorial waters. There are tax rulings stipulating that mobilization/demobilization charges are taxable under the presumptive taxation regime. It may however be possible to claim exemption under a tax treaty to the extent mobilization/demobilization is undertaken beyond the territorial waters of India.

2.5 Deductions and allowances

The deduction available to domestic companies for most revenue expenses is subject to certain restrictions/limitations. Deduction is not available for certain expenses on which withholding tax has not been applied, payment of statutory dues after the prescribed due dates and payments towards fines and penalties, etc.

Depreciation is allowed at prescribed rates for capital expenditure resulting in the creation of assets other than land. Certain specified capital expenses are eligible for amortisation. For instance, preliminary or pre-operative expenses are eligible for amortisation over a period of five years. The capital expenses which neither result in the creation of a capital asset nor are eligible for amortisation are disallowed.

Notwithstanding the general rules above, companies engaged in the exploration for and exploitation of oil and gas are eligible to deduct certain expenditure in accordance with the special income computation provision provided in the domestic tax legislation, and Model Production Sharing Contract. These are discussed below:

Nature of expenses allowable as per the latest Model Production Sharing Contract (under New Exploration Licensing Policy IX)	Period in which deduction is granted
Revenue and capital expenditures incurred in respect of exploration and drilling operations, (including drilling during the course of production operations)	100% in the year of commercial production; or amortised over ten years from the date of first commercial production
Expenses during development operations (other than drilling operations)	In the year when incurred in accordance with the general rules as detailed in Section 2.5
Unsuccessful exploration costs incurred in the pre-production period i.e. exploration costs which do not result in any commercial discovery in the contract areas, incurred before and up to the date of commencing commercial production	100% in the year of commercial production; or amortised over ten years from the date of first commercial production
Unsuccessful exploration costs incurred in the post-production period i.e. exploration costs which do not result in any commercial discovery in the contract areas, incurred after the date of commencing commercial production	In the year when incurred

If any of the above expenses are incurred in conjunction with any other business, only the proportionate expenses which could be substantiated as a fair proportion attributable to the business of prospecting, extraction or production of petroleum and natural gas are allowable.

There are tax rulings stipulating that mobilization/demobilization charges are taxable under the presumptive taxation regime. It may however be possible to claim exemption under a tax treaty to the extent mobilization/demobilization is undertaken beyond the territorial waters of India.

Field allowances were introduced in 2009 to provide an incentive for development of commercially marginal oil and gas fields.

2.6 Losses

Losses of domestic companies can be carried forward and set off against future revenue for a maximum of eight assessment years from the year in which the loss was first computed. Unabsorbed depreciation is treated distinctly from losses and can be carried forward for an indefinite period.

A closely held company must satisfy a 51% continuity of ownership test to qualify for business loss carried forward. A company in which the public are not substantially interested may be considered to be a closely held company. Generally speaking, a listed company or its subsidiary, would be a company in which the public are substantially interested.

2.7 Foreign entity taxation

Foreign entities are taxed on the income that accrues or arises in India, is deemed to accrue or arise in India, or is received or deemed to be received in India.

Foreign entities engaged in the exploration, extraction, or production of oil and gas assets may constitute a permanent establishment in India. Income attributable to the permanent establishment would be taxable in India. The income computation mechanism, including deduction of expenses, as discussed earlier for domestic companies, would also apply to non-residents.

There is a special tax regime for foreign companies that are engaged in the business of providing services or facilities, or supplying or hiring plant or machinery used in connection with the prospecting, extraction or production of petroleum and natural gas. Under this regime, 10% of the amounts received as consideration for the aforesaid services is taxable on a presumptive basis (i.e. the taxable income is computed as a percentage of gross income, without any regard to actual expenses incurred in earning the income).

Please refer Section 1.0 – Summary – for the Indian tax rates as applicable to foreign companies.

For non-corporates such as Association of Persons, Body of Individuals, unincorporated entities, etc., the maximum applicable basic rate is 30%. However, if a foreign company is a member of an Association of Persons, Body of Individuals or unincorporated entities, the maximum marginal rate of 40% will apply on the share of that foreign company. This basic rate may be increased by a surcharge and an education cess.

3.0 Other corporate income tax

3.1 Minimum alternate tax

Minimum alternate tax (MAT) applies to a company if the tax payable on its total income as computed under the tax laws is less than 18.5% of its “book profit”. ‘Book profit’ means the net profit as per the profit and loss account of the company subject to certain adjustments specified in the law. If MAT applies, the tax on total income is deemed to equal 18.5% of the company’s book profit. This is further increased by a surcharge and an education cess.

Please refer Section 1.0 – Summary for MAT rates.

Credit is available in respect of tax paid under the MAT against the tax payable for subsequent years. MAT credit can be carried forward for ten years and may be set off against normal income tax payable under domestic tax provisions.

3.2 Dividend distribution tax

Dividends distributed by domestic companies are subject to dividend distribution tax (DDT) at the basic rate of 15%. This is further increased by a surcharge and an education cess. The surcharge is 10% and the education cess is 3%. Therefore, the effective DDT rate is 16.995%.

The domestic tax laws provide that dividends liable to DDT shall be reduced by the amount of dividends received by the domestic company during the financial year. The reduction is available if the dividend is received from the domestic subsidiary company and it has paid DDT. From 1 June 2013, the benefit of reduction is also extended to the dividend received from a foreign subsidiary company provided tax is payable on such dividend income by the domestic company at the concessional tax rate. The above benefit will only be available up to 31 March 2014 unless extended as the concessional tax rate on dividend income received from a foreign subsidiary company is applicable only up to 31 March 2014.

3.3 Tax on the distributed income of domestic company for buy-back of shares

In the case of a buy-back of shares from an unlisted company, the company purchasing its own share is required to pay additional income-tax of 20% on distributed income. This is further increased by a surcharge and an education cess. The surcharge is 10% and the education cess is 3%. Therefore, the effective tax rate is 22.66%. The distributed income means the consideration paid by the company upon purchase of its own shares as reduced by the sum received by the company at the time of issue.

The income arising to the shareholder in respect of such a buy-back by the company will be exempt where the company is liable to pay the additional income-tax on the buy-back of shares.

3.4 Wealth tax

Wealth tax is chargeable on the taxable net wealth in excess of INR 3 million in a year at the rate of 1% and applies to both domestic and foreign companies. Net wealth means the amount by which the aggregate value, computed in accordance with the provisions of the Wealth Tax Act, of all the taxable assets belonging to the assessee on the valuation date exceeds the aggregate value of all the debts owed by the assessee in relation to the said assets. Broadly, taxable assets are urban land, buildings or appurtenant land, motor cars, yachts, boats, aircrafts etc. Wealth tax is not levied on foreign companies in respect of assets located outside India.

4.0 Tax incentives

4.1 Profit-linked incentives

A tax holiday is available for an undertaking which (a) begins commercial production of mineral oil on or after 1 April 1997 and where the contract is awarded before 1 April 2011; or (b) which begins commercial production of natural gas on or after 1 April 2009 from the blocks licensed under:

- (i) the VIIIth round of bidding for award of exploration contracts under the National Exploration Licensing Policy; or
- (ii) the IVth round of bidding for award of exploration contracts under the Coal Bed Methane Blocks.

A tax holiday is also available for an undertaking engaged in the business of refining mineral oil where the refining commences between 1 October 1998 and 31 March 2012.

The tax holiday is in the form of deduction equal to 100% of profits generated during a period of seven consecutive assessment years starting from the year in which the undertaking commences the commercial production or refining of mineral oil.

4.2 Investment-linked incentives

Companies engaged in laying and operating a cross-country natural gas pipeline network for distribution, including storage facilities, are eligible for investment-linked incentives if it commences its operations on or after 1 April 2007. This enables a company to claim an outright deduction, in the year in which operations are commenced, for the expenditure incurred prior to commencement of business and the amount capitalised in the books on the date of commencement of operations.

Companies engaged in the business of manufacture or production of any product which acquire and install new asset being plant and machinery between 1 April 2013 up to 31 March 2015, will be eligible for a one time investment allowance of 15% in the year where the aggregate value of assets purchased exceeds INR 1,000 million. Certain items such as office appliances, computers, vehicles, etc. will not be eligible for the deduction.

4.3 Research and development

In addition to the revenue expenditure which is allowable under the general domestic tax provisions, specified capital expenditure relating to research is allowed an outright deduction in the year in which it is incurred. Where a company is engaged in the manufacture or production of a product and incurs expenditure on research, including capital expenditure, a deduction of 200% of the revenue and capital expenditure may be allowed. The benefit of deduction of 200% is available to the company undertaking research in an in-house research and development facility which is approved by the Secretary, Department of Scientific & Industrial Research, Government of India.

Companies engaged in laying and operating a cross-country natural gas pipeline network for distribution, including storage facilities, are eligible for investment-linked incentives if it commences its operations on or after 1 April 2007.

4.4 Other incentives

Companies engaged in the exploration, extraction and production of petroleum and natural gas are allowed to deduct contributions made to a Site Restoration Fund. The funds accumulated in a Site Restoration Fund are used to meet the expenditure to be incurred on the expiry or termination of the Production Sharing Contract, or relinquishment of part of the contract area towards necessary site restoration and other expenses to prevent hazards to life or property or environment. The deduction will be restricted to the lower of the following:

- the amount deposited in a bank account maintained with the State Bank of India or "Site Restoration Fund" in accordance with a Government-approved scheme; or
- 20% of the profits of the business for the relevant financial year.

5.0 Payments to related parties

5.1 Transfer pricing

When the income/allowance of a non-resident in respect of transactions with residents/non-residents associated enterprises is taxable in India, then such income is subject to transfer pricing regulations in India. Any income/allowance for expense arising from an "international transaction" shall be computed having regard to the arm's length price. 'International transaction' is defined as a transaction between two or more associated enterprises, either or both of whom are non-residents.

The arms' length price is to be determined by one of the following methods:

- comparable uncontrolled price method;
- resale price method;
- cost plus method;
- profit split method;
- transactional net margin method; and
- such other method as may be prescribed by the Central Board of Direct Taxes.

Every person who has entered into an international transaction is required to keep and maintain prescribed information and documentation, and obtain a report from a practicing chartered accountant in India setting forth the prescribed particulars. The report is required to be electronically sent to the tax officer. The report is required to be filed on or before November 30 of the following tax year.

An advance pricing agreement mechanism has been introduced with effect from 1 July 2012.

From 1 April 2012, transfer pricing regulations are applicable to certain specified domestic transactions. The following transactions are covered:

- (i) Expenditure for which payment is made or to be made to specified domestic related parties.
- (ii) Transfer of goods or services between a tax holiday undertaking and non-tax holiday undertaking.
- (iii) Business transactions between an eligible business (tax holiday unit) and other persons producing more than ordinary profits owing to close connection or otherwise.

The domestic related party inter alia includes a director, a relative of a director, a person having substantial interest in the taxpayer (carrying not less than 20% of the voting power), and fellow related parties where a single person has substantial interest in two taxpayers.

Every person who has entered into an international transaction is required to keep and maintain prescribed information and documentation, and obtain a report from a practicing chartered accountant in India setting forth the prescribed particulars.

5.2 Thin capitalization

The Indian Income Tax Act does not prescribe any thin capitalization rules. However, the Indian exchange control regulations stipulate the debt-equity ratio in respect of borrowings obtained from foreign equity holders. Currently, the permissible debt-equity ratio is 4:1 in respect of borrowings obtained from foreign equity holders in excess of USD 5 million for specified purposes including investments in the infrastructure sector (comprising mining, exploration and refining).

5.3 Interest deductibility

The interest paid on the amount borrowed for the purpose of carrying on the business is deductible in computing taxable income. However, if the amount borrowed is invested to earn tax-free income e.g. dividends etc., then interest would be disallowed. The law provides a specific computation mechanism for determining such disallowances.

6.0 Transactions

6.1 Capital gains

Income arising on the transfer of a capital asset is subject to capital gains tax. The definition of a capital asset is wide and encompasses property of any kind held by the taxpayer whether or not connected to its business or profession. Capital assets can be classified into long and short-term capital assets based on the period of holding of the assets. Capital assets held for more than three years are classified as long-term capital assets, except for certain specified securities. Specified securities include shares held in a company, any securities listed on a recognized stock exchange in India and units of mutual fund, etc. These securities are required to be held only for more than one year to be classified as a long-term capital asset.

Capital gains arising on the transfer of a capital asset are computed as the difference between the full value of consideration received in connection with the transfer of an asset and the cost of acquisition/improvement. Expenses incidental to the transfer of the asset are also permitted to be deducted in arriving at the taxable capital gains. The cost of acquisition in the case of long-term capital assets is indexed. The indexation is a process of increasing the cost basis of an asset having regard to the cost inflation index of the asset in the year when it was purchased and in the year when it is sold.

Capital gains arising on the transfer of depreciable assets are considered as short-term capital gains (and not as revenue income).

The tax rates applicable to capital gains are as follows:

- Long-term capital gains are generally taxable at the rate of 20% (with cost indexation) for both domestic and foreign companies. Long-term capital gains arising on the transfer of listed securities are exempt from tax if the sale is on the Indian stock exchange and Securities Transaction Tax is paid. In some circumstances and depending on residency of the seller, if the sale of listed securities is outside the stock exchange, the applicable tax rate is 20% with indexation or 10% without indexation. The applicable tax rate in the case of non-residents on the sale of unlisted securities is 10%. There is some debate whether capital gains on the sale of shares of a private company are eligible for a tax rate of 10% as such shares may not be considered as "securities".
- Short-term capital gains are taxable at the rate of 30% for domestic companies and 40% for foreign companies. A lower rate of tax of 15% is applicable in respect of short-term capital gains arising on the sale of securities on stock exchanges in India.

The above rates are to be increased by a surcharge and an education cess.

6.2 Sharing arrangements and farm outs

Consideration received upon farm out which involves the recoupment of expenses already allowed as a deduction is treated as business profits. The consideration in excess of costs may be characterised as capital gains. Please refer Section 6.1 for the computation of capital gains and tax rates thereon.

Capital gains arising on the transfer of a capital asset are computed as the difference between the full value of consideration received in connection with the transfer of an asset and the cost of acquisition/improvement.

7.0 Withholding taxes

7.1 Dividends

As a domestic company pays DDT on dividends distributed, dividends are exempt in the hands of the shareholder, whether resident or not.

7.2 Interest

Interest payable by a resident is subject to withholding tax as follows:

- (a) Interest payable to Indian residents will be subject to withholding of tax at the rate of 10%.
- (b) Interest payable to non-residents on accounts of debt incurred by the Government or an Indian company in foreign currency will be subject to withholding tax at the rate of 20%.
- (c) Interest payable to non-residents on account of debt incurred by an Indian company in a foreign currency will be subject to withholding tax at the rate of 5% if the loan agreement is approved by the Central Government of India, and the monies are borrowed between 1 July 2012 and 30 June 2015.
- (d) Interest payable to non-residents (whether or not they have a permanent establishment in India) on account of other debts will be subject to withholding tax at the rate of 40% where the non-resident is a corporate, and 30% where the non-resident is not a corporate.

The above rates are to be increased by a surcharge and an education cess.

The withholding tax rates on payments to non-residents may be reduced to a lower rate as prescribed under the tax treaty. The tax treaty benefits will be available to non-residents if the non-resident obtains a valid Tax Residency Certificate from the Government of a foreign country and also executes a declaration in prescribed Form 10F.

The withholding tax rate will be increased to 20% (in the cases covered in c above) if the recipient does not furnish the tax registration number (known locally as the Permanent Account Number) to the payer of the income.

7.3 Royalties

A royalty payable by a resident is subject to withholding tax at the rate of 10% where the recipient is resident and 25% where the recipient is a non-resident. The rate will be increased by a surcharge and an education cess.

The withholding tax rates on payments to non-residents may be reduced to a lower rate as prescribed under the tax treaty. The lower rate prescribed under the tax treaty will not be applicable if the recipient does not supply the tax registration number (locally known as Permanent Account Number) to the payer of the income. The withholding tax rate in such a case will be 20%.

7.4 Foreign tax treaties

India has entered into several income tax treaties with other countries, potentially allowing for a reduction in withholding tax rates and providing other fiscal benefits. Where the provisions of the domestic law are inconsistent with the treaty, the more favorable provision may be applied.

8.0 Indirect taxes

Indirect taxes are applicable on a range of transactions including imports, manufacture, trade, distribution and services etc.

India has a federal system of taxation wherein the Central (Federal) and State (Provincial) Governments levy taxes on goods and services based on the taxable event. The indirect taxes levied by a Central Government are central excise, customs duty, service tax and central sales tax. Additionally, the State Government and municipalities also levy indirect taxes such as value-added tax, entry tax, octroi duty and local body tax.

8.1 Service tax

Service tax is payable at 12.36% (including the education cess) on the provision of specified taxable services in India. Recently, the Government of India has broadened the levy of services tax to all transactions except those identified in the "negative list" or specifically exempted.

Interest payable to non-residents on accounts of debt incurred by the Government or an Indian company in foreign currency will be subject to withholding tax at the rate of 20%

Typically, the service provider is liable to collect and remit service tax. However, in respect of specified transactions, such as the transportation of goods by road, the provision of services by a service provider outside India and sponsorship services etc., the service recipient is required to make the payment of service tax. However, service tax need not be paid on exports of services, provided prescribed conditions are satisfied. Service tax legislation further provides exemptions/effective concessional rate for specified transactions like the construction of roads and works contract etc. The service provider should factor in the optimum tax rate as the service recipient may not always be eligible to avail CENVAT credit of taxes paid on inputs.

A service provider can also/offset service tax paid on input services and notified duties on inputs and capital goods, subject to meeting certain conditions. The credit/set off provisions are contained in CENVAT Credit Rules ("CCR") and are subject to a number of conditions and restrictions as prescribed under the said rules.

8.2 Customs duties on import and export:

Customs duty is levied by the Central Government on the import of goods into India. It is payable by the importer. Duty is also levied on the export of few specified goods.

Customs duty on import comprises of basic customs duty ("BCD"), additional customs duty ("ACD") and special additional duty ("SAD"), plus applicable cess.

BCD is levied on the assessable value of the imported goods determined in accordance with the terms of the Customs Valuation Rules ("CVR"). ACD, which is levied in lieu of excise duty, is computed on the CVR assessable value plus BCD.

SAD is levied in lieu of VAT/sales tax at the rate of 4% on the aggregate of CVR assessable value, BCD and ACD. In addition, an education cess at 3% is also charged on the aggregate of BCD and ACD.

Peak rate of customs duty is 28.85% on cost, insurance and freight ("CIF") value plus a 1% handling charge.

The applicable rates are determined based on the classification under the Customs Tariff which is aligned with the international Harmonised System of Nomenclature developed by the International Customs Organisation and are applied on the assessable value of imported goods.

A credit in respect of ACD and SAD is available to a manufacturer for set-off against excise duty payable on output, subject to conditions. Further, a credit in respect of ACD is available to a service provider for set-off against service tax payable on output services under the terms of the CCR. An importer-trader is also eligible to claim exemption from SAD on the import of goods, which require affixation of MRP, or the refund of SAD, where VAT is paid on the sale of the same subject to conditions.

Various exemptions or concessions are available on the basis of classification and end use of the imported products. Concessions are also available for setting up industrial plant, infrastructure projects (e.g. power, irrigation, mining, etc.), exploration of oil and other minerals, and other specified projects contributing to the economic development of India.

A concessional rate of customs duty is also available for the import of goods from specific countries with whom India has executed bilateral/multi-lateral treaties. The Government of India has entered into several free or preferential trade agreements with trade partners such as Thailand, Sri Lanka, the South Asian Association for Regional Cooperation (SAARC) countries, Singapore and other countries comprising the Association of Southeast Asian Nations (ASEAN). Further, the Government of India is also negotiating trade agreements with European Union countries, MERCOSUR countries (Argentina, Brazil, Paraguay and Uruguay) and others.

8.3 Excise tax

Central excise duty is levied on the manufacture of excisable goods in India. The peak rate of central excise duty, inclusive of an education cess, is 12.36%.

Central excise duty is broadly based on value added principles, whereby the manufacturer is eligible to an avail of a credit in respect of specified taxes/duties paid on eligible inputs/capital goods and input services, subject to meeting certain conditions and procedural compliance. However, credit of duties paid on motor spirit, high diesel oil and light diesel oil used in the manufacture of goods cannot be availed.

Peak rate of customs duty is 28.85% on cost, insurance and freight ("CIF") value plus a 1% handling charge.

Various end-user based concessions/exemptions are available based on:

- manufacturing in notified backward regions is encouraged by granting concessions/exemptions on goods manufactured there;
- exemptions/concessions are also extended to goods manufactured to cater for the export market or for certain notified projects; and
- specified oil and gas products like crude, superior kerosene oil (SKO), LPG etc.

8.4 VAT, GST and Sales & Use

VAT is levied on the sale of goods within the State and each State has its own legislation in this regard. Sales involving the movement of goods from one State to another are governed by a central legislation called the Central Sales Tax (CST) Act which is uniformly applicable to all States.

The VAT rate is divided into two components – a general rate of 4% to 5% and a residual rate of 12% to 15% which varies across the States. However, there is a third category of higher VAT rates applicable to specific products, which ranges from 15% to 33%. Petroleum products such as petrol, diesel and aviation turbine fuel (ATF) fall within this category.

The benefit of a concessional rate of 2% CST can be availed on the inter-state sale of goods, which are used in manufacturing, mining, generation and distribution of power, resale, etc. subject to production of declarations prescribed in the legislation. In the absence of a concessional rate of CST, the rate applicable on the sale of goods in the dispatching State would be applicable.

A registered dealer can adjust the VAT paid on goods purchased locally in the State against his VAT and CST liability on sales. However, VAT credit is normally not allowed on petroleum products in most States. There are States, which allow such credit on specified petroleum products which are resold.

GST is scheduled to replace the current scheme of indirect taxation. Its implementation will lead to the abolition of a series of other indirect taxes such as central excise, service tax, CST, VAT and entry tax, thus mitigating multiple layers of taxation currently in existence. GST is a comprehensive tax on the manufacture, sale and consumption of goods and services and will have a dual structure – Central GST and State GST. Both the Central and the State governments will concurrently levy GST and credit would be available thereon for adjustment against the Central GST and State GST respectively.

However, it is widely expected that crude petroleum, diesel, petrol and aviation turbine fuel would not come under the purview of GST. Drafting of the model legislation for Central and State GST is in progress and the Goods & Services Tax Network ('GSTN') for implementing IT infrastructure and containing an online portal for GST registration, return submission and tax payment is expected to be operational by 2015.

9.0 Other

9.1 General anti-avoidance rules

From 1 April 2015, the General Anti-Avoidance Rules will apply. Under these rules, an arrangement entered into by a taxpayer may be declared as an impermissible avoidance arrangement if the main purpose is to obtain a tax benefit and which satisfies at least one of the following four tests:

- it creates rights or obligations of the parties which are not at arm's length;
- it results directly or indirectly in misuse or abuse of any provisions of the Indian Income Tax Act;
- it lacks commercial substance or is deemed to lack commercial substance in whole or in part; and
- it is entered into or carried out, by means, or in a manner, not for a bona fide purpose.

The VAT rate is divided into two components – a general rate of 4% to 5% and a residual rate of 12% to 15% which varies across the States.

The tax consequences of the impermissible avoidance arrangement will be determined in such a manner as is deemed appropriate in the circumstances of the case, including inter alia the following:

- disregarding, combining or recharacterising any step in the arrangement, whether in part or in whole;
- ignoring the arrangement;
- disregarding or combining any accommodating party or other party to the arrangement;
- deem the persons who are connected person in relation to each other to be one and the same person;
- reallocating, amongst the parties to the arrangement, any accrual or receipt of a capital or a revenue nature or any expenditure, deduction relief or rebate;
- determining the place of residence of a party, or the situs of an asset or transaction other than as provided for in the arrangement; and
- considering and looking through the arrangement by disregarding any corporate structure.

9.2 Controlled foreign corporations

In addition, the Direct Taxes Code proposes to introduce Controlled Foreign Corporations regulations. A resident would be deemed to exercise control over a Controlled Foreign Company if:

- (a) It holds more than 50% of the voting power, share capital, income, or assets of the company; or
- (b) It exercises a dominant influence on the company arising from a special contractual relationship or decisive influence in a shareholders meeting.

Income attributable to the Controlled Foreign Corporation would be taxed in the hands of the resident.

The Direct Taxes Code is still at the proposal stage. The enactment of the Direct Taxes Code is currently at discussion stage.

9.3 Royalty/profit sharing

Exploration of oil and natural gas under the New Exploration Licensing Policy Ninth Round (NELP-IX)

The Government of India invites offers for oil and gas blocks in India. The successful bidder would be required to enter into a Production Sharing Contract which is based on the Model Production Sharing Contract (MPSC). Under the MPSC, the contractor is required to pay a royalty and share the profit petroleum with the Government.

Royalty

The royalty with respect to offshore areas is payable to the Central Government whereas the royalty with respect to onshore areas is payable to the respective State in which such area is located. The royalty in respect of oil and gas blocks allotted under the NELP-IX is payable as follows:

Areas	Percentage	Value
Offshore areas	10%	Well-head value of crude oil and natural gas
Onshore areas	12.5%	Well-head value of crude oil
	10%	Well-head value of natural gas
Offshore area [beyond four hundred (400) meters isobaths]	5% for the first seven years from the date of commencement of commercial production in the field and thereafter 10%	Well-head value of crude oil and natural gas

The royalty amount due to Central/State Governments shall be payable by the end of the succeeding month at the latest.

Profit petroleum

Profit Petroleum means the total value of petroleum produced and saved from the contract area in a particular period and reduced by 'Cost Petroleum'.

Profit Petroleum from the contract area in any year shall be shared between the Government and the contractor based on the biddable pre-tax investment multiple achieved by the contractor. The profit petroleum share of the Government is biddable by the contractor.

The Government of India invites offers for oil and gas blocks in India. The successful bidder would be required to enter into a Production Sharing Contract which is based on the Model Production Sharing Contract (MPSC).

Cost Petroleum means the portion of the total value of petroleum produced and saved from the contract area which the contractor is entitled to take in a particular period for the recovery of 'contract costs'.

Costs incurred by the contractor on the petroleum operations as per the work program and budget reviewed and approved by the management committee shall be allowable.

Contract costs means exploration costs, development costs and production costs which are allowed to be cost recoverable. The contractor shall be entitled to recover in full during any year, the royalty payments to the Central/State Governments in that year out of the cost petroleum.

Subject to provisions of the Production Sharing Contract, contributions made to any site restoration fund scheme formulated by the Government shall be cost recoverable, including but not limited to, sinking funds established for the abandonment and restoration of the contract area.

The amount of allowable cost which cannot be recovered in a given year can be carried forward to subsequent years until the time the entire cost recovery is achieved.

The costs and expenses which are not recoverable or allowable for cost recovery are as follows:

- (i) Costs and charges incurred before the effective date of the Production Sharing Contract including costs in respect of preparation, signature or ratification of the contract.
- (ii) Expenditures in respect of any financial transaction to negotiate, float or otherwise obtain or secure funds for petroleum operations including, but not limited to, interest, commission, brokerage and fees related to such transactions, as well as exchange losses on loans or other financings.
- (iii) Costs of marketing or transportation of petroleum beyond the delivery point.
- (iv) Expenditures incurred in obtaining, furnishing and maintaining the guarantees required under the contract and any other amounts spent on indemnities with regard to non-fulfillment of contractual obligations.
- (v) Attorney's fees and other costs and charges in connection with arbitration proceedings and sole expert determination pursuant to the Production Sharing Contract.
- (vi) Fines, interest and penalties imposed by the courts.
- (vii) Donations and contributions.
- (viii) Expenditures on the creation of any partnership or joint venture arrangement.
- (ix) Amounts paid with respect to the non-fulfillment of contractual obligations.
- (x) Costs and expenditures incurred as a result of misconduct or negligence of the contractor.
- (xi) Expenses of the members of the management committee.
- (xii) Financing cost of inventory, loss on disposal of inventory.
- (xiii) Costs which are not adequately supported and documented.

9.4 Choice of business entity

The incorporation of a local company is not mandatory for carrying out prospecting, exploration or production of petroleum or natural gas in India. The contract area where the foreign company carries out prospecting, exploration or production of petroleum or natural gas may be regarded as a place of business in India and will require registration with the Reserve Bank of India.

If a consortium of Indian companies and foreign companies is formed in order to bid for the licenses for carrying out prospecting, exploration or production of petroleum or natural gas, the members of the consortium are taxed individually and not as an association of persons, and the tax rate applied to each member will be the rate applicable to each member in the consortium based on its circumstances.

9.5 Foreign currency

The functional currency in India is Indian Rupees. Unless otherwise permitted, an Indian resident is not allowed to acquire, hold, own, possess or transfer any foreign currency under Indian exchange control regulations. Dealings in foreign currency are permissible for specified current and capital account transactions.

Costs incurred by the contractor on the petroleum operations as per the work program and budget reviewed and approved by the management committee shall be allowable.

10.0 Oil and gas contact information

India (GMT +5.5)

Deloitte Haskins & Sells

IndiaBulls Finance Centre,
Tower 3, 28th Floor,
Senapati Bapat Marg, Elphinstone Road (W)
Mumbai – 400013
Telephone: +91 (22) 6185 4000

Sunil D. Shah

Tax Partner-Oil & Gas Tax
Telephone: +91 (22) 6185 4140
sunilshah@deloitte.com

About Deloitte

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee (“DTTL”), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as “Deloitte Global”) does not provide services to clients. Please see www.deloitte.com/about for a more detailed description of DTTL and its member firms.

Deloitte provides audit, tax, consulting, and financial advisory services to public and private clients spanning multiple industries. With a globally connected network of member firms in more than 150 countries, Deloitte brings world-class capabilities and high-quality service to clients, delivering the insights they need to address their most complex business challenges. Deloitte has in the region of 200,000 professionals, all committed to becoming the standard of excellence.

The Deloitte Touche Tohmatsu Limited (DTTL) Global Energy & Resources group, which includes senior partners from Deloitte member firms around the world, provides comprehensive, integrated solutions to the energy sector. These solutions address the range of challenges facing energy companies as they adapt to changing regulatory environments, to political, economic and market pressure, and to technological development. Deloitte member firms’ in-depth knowledge in this dynamic sector serves as a valuable resource for a significant portion of the world’s largest energy companies. Deloitte member firms provide the energy industry with unparalleled service, innovation, and critical thinking.

This publication contains general information only, and none of Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively the “Deloitte Network”) is, by means of this publication, rendering professional advice or services. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser. No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this publication.

© 2014. For information, contact Deloitte Touche Tohmatsu Limited.

Designed and produced by The Creative Studio at Deloitte, London. 35647A